# LEGISLATIVE SERVICES AGENCY
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## FISCAL IMPACT STATEMENT

**LS 7387** **NOTE PREPARED:** Jan 8, 2013
**BILL NUMBER:** SB 521 **BILL AMENDED:**

**SUBJECT:** Indiana New Markets Job Act.

**FIRST AUTHOR:** Sen. Head **BILL STATUS:** As Introduced
**FIRST SPONSOR:**

**FUNDS AFFECTED:** X **GENERAL** **IMPACT:** State
X **DEDICATED**
**FEDERAL**

**Summary of Legislation:** This bill creates the Indiana New Markets Job (INMJ) Tax Credit which is similar to the Federal New Markets Tax Credit. The bill requires a Qualified Community Development Entity to pay a conditionally refundable fee of $500,000 and a nonrefundable application fee of $5,000 for each Qualified Equity Investment (QEI) that the entity seeks to have approved by the Indiana Economic Development Corporation (IEDC). The IEDC may not approve more than $20 M in QEI per state fiscal year.

The bill provides that the IEDC is required to issue letter rulings requested by taxpayers, similar to private letter rulings issued by the Internal Revenue Service at the federal level, regarding the INMJ that will bind the Department of State Revenue, the IEDC, it's agents, and their successors.

**Effective Date:** January 1, 2013 (retroactive).

**Explanation of State Expenditures:** *Department of State Revenue (DOR):* The DOR will incur some administrative expenses relating to the revision of the tax form instructions and software programs to implement this bill. The DOR's current level of resources should be sufficient to implement the program.

*Indiana Economic Development Corporation:* The IEDC will incur additional expenses to establish this program. The IEDC will be required to develop an application, process applications, certify community investments, and monitor investment projects. The IEDC will process all the fees paid by the applicants as defined within the bill. The IEDC's current level of resources should be sufficient to implement the program.

The bill also requires the IEDC to issue letter rulings to taxpayers regarding the INMJ credit. A letter ruling is a written interpretation of tax law issued to a private individual. The bill states the IEDC has 60 days to respond to a request, but the IEDC may decline for good cause. The letter ruling binds the DOR, the IEDC, and it's agents until the taxpayer claims all the taxpayer's IMNJ credits. In addition, the letter ruling only applies to the requesting taxpayer. The IEDC's current level of resources should be sufficient to provide letter rulings.

**Explanation of State Revenues:** *Summary*- The Indiana New Markets Job Tax Credit is designed to attract private investments in economically distressed neighborhoods. The total credit equals 39% of the Qualified Equity Investment (QEI) made by a qualified Community Development Entity (CDE) and is claimed over a seven-year period. Each year, the taxpayer applies the appropriate percentage to the QEI to determine the annual credit amount:

1. 0% for the first and second year
2. 7% for the third year
3. 8% for the fourth, fifth, sixth, and seventh year

The bill goes into effect in CY 2013. INMJ credits can be awarded for QEIs made in that year. The fiscal impact of credits awarded in CY 2013 will occur in FY 2016 due to the applicable percentage tiers. The estimated revenue loss in FY 2016 is approximately $1.4 M with the estimated revenue loss totaling $3.0 M in FY 2017. The usage of the credit is limited based on the QEI certified by the IEDC. The bill limits the QEI that can be certified each year to $20 M per fiscal year.

A portion of the revenue loss may be offset by an indeterminable amount of fee revenue received. All applicants must pay a nonrefundable application fee of $5,000, which is deposited in the state General Fund. Applicants also must pay a conditionally refundable $500,000 performance fee. If this fee is not refunded to the qualified CDE it is deposited in the state General Fund as well.

*Background* - Applicants are required to pay a $5,000 fee when applying to the IEDC. This fee is deposited in the state General Fund. The applicant is also required to pay a $500,000 conditionally refundable fee to the IEDC. The refundable fee is placed into the New Markets Performance Guarantee Fund. The $500,000 will be returned to the taxpayer upon meeting the investment conditions before the second credit allowance date. If the taxpayer fails to meet the conditions, the fee is transferred to the state General Fund.

The credit can be used to offset tax liabilities from the Individual Adjusted Gross Income Tax, Corporate Adjusted Gross Income Tax, Financial Institutions Tax, and Insurance Premiums Tax. Revenue collected from those taxes is deposited in the state General Fund. The credit is nonrefundable, but the taxpayer may carry forward unused credits to subsequent years. The credit may not be carried back or transferred. In addition, the IEDC must limit the amount of approved QEIs to a total of $20 M per fiscal year.

The Center for Business and Economic Research at Ball State University conducted a study on the effectiveness of the federal New Markets Tax Credit Program (NMTC) and how a state-level version of the NMTC affected overall levels of investment. The study found that states with their own version of a New Markets Tax Credit had higher levels of NMTC investments. They ran a simulation on the impact of Indiana implementing a 39% state version of the NMTC. The simulation estimated that an Indiana New Markets program would attract $433 M dollars in investments over a seven-year period. That is an average of $61 M QEIs a year.

However, the model results were based on the federal NMTC. The IMNJ credit has some slight differences. First, it has an expanded business eligibility criteria. The definition of a low-income community for the federal program is based solely on median family income. The IMNJ credit includes those communities and any county where the average annual unemployment rate is higher than the statewide average unemployment rate. Also, the federal program does not require fees to apply for the credit.

Assuming Indiana attracts the maximum allowable QEI of $20 M per year beginning in tax year 2013, the first year the IMNJ credits for those investments may be used to offset a tax liability would be FY 2016. This is due to the applicable credit percentage tiers. The IMNJ credit amount is spread over a seven-year period.

The taxpayer may not use the IMNJ credit for the first two years following the qualifying investment. Then, the credit equals 7% of the qualifying investment in year three and 8% of the qualifying investment in year four, five, six, and seven. So, the last year an IMNJ tax credit could be claimed for a qualifying investment made in tax year 2013 would be tax year 2019, with the fiscal impact of that last year's credit occurring in FY 2020. If $20 M in QEI is authorized each year between CY 2013 and CY 2017, the maximum annual revenue loss of $7.8 M would occur beginning in FY 2020.

*Additional Background-Federal New Markets Tax Credit Program:* This bill is based on the NMTC Program. The program was enacted by Congress as part of the Community Renewal Tax Relief Act of 2000 and is incorporated as section 45D of the Internal Revenue Code. This Code section permits individual and corporate taxpayers to receive a credit against federal income taxes for making qualified equity investments (QEIs) in qualified community development entities (CDEs).

These investments are expected to result in the creation of jobs and material improvement in the lives of residents of low-income communities. Examples of expected projects include financing small business, improving community facilities such as daycare centers, and increasing home ownership opportunities. The INMJ credit uses the same language to determine a qualifying project, except the Indiana program excludes charter schools and businesses who derive over 15% of their annual revenue through the rental or sale of real estate.

The actual cash investment made by the investor to the CDE, which is referred to as the equity investment, is the first step in defining a QEI. The cash investment eventually qualifies for the NMTC provided that the CDE makes qualified low-income community investments.

A QEI is, in general, any equity investment in a CDE if:

(1) Such investment is acquired by the investor at its original issue (directly or through an underwriter) solely in exchange for cash;
(2) Substantially all (at least 85%) of the cash is used by the CDE to make a qualified low-income community investment; and
(3) The investment is designated CDE as a QEI on its books and records using any reasonable method.

A taxpayer holding a qualified equity investment on a credit allowance date occurring during the taxable year may claim the NMTC for such taxable year in an amount equal to the applicable percentage of the original purchase price of the QEI. The credit period for the investment is the seven-year period beginning on the date a QEI is initially made, even though the credit is allowable on the first day of each credit year.

**Explanation of Local Expenditures:**

**Explanation of Local Revenues:**

**State Agencies Affected:** DOR; IEDC.

**Local Agencies Affected:**

**Information Sources:** Hicks, Michael J. And Dagney Faulk. "*The Effect of State-Level Add-On Legislation to Federal New Market Tax Credit Program.*" February 2012; Internal Revenue Service, "*New Markets Tax Credit.*" May 2010; Community Development Financial Institutions Fund, U.S. Department of the Treasury, http://www.cdfifund.gov/what_we_do/programs_id.asp?programID=5

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